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TAGS: ECON ETRD EFIN TH VN
SUBJECT: THAILAND WARILY WATCHES VIETNAM'S ECONOMIC RISE

¶1. Summary: A long string of bad economic news from Thailand coupled with a seemingly non-stop slew of positive news out of Vietnam has sparked great angst from Thai business and government officials that the country will soon fall behind their rapidly growing neighbor. Thai economic analysts fear that Vietnam's increasing economic power will spell added competition for Thailand in their traditional export markets, and could siphon off much foreign investment that would otherwise have come to Thailand. The RTG is meeting the trade challenge by focusing on cooperation with the Vietnamese rather than competition. Additionally, despite the recent missteps, Thailand maintains certain competitive advantages that will likely keep much current investment here, but faces the prospect of a downturn in new investment that may flow to Vietnam in its place. End summary.

¶2. On January 9 the RTG announcement its intention to toughen rules on foreign investment in certain sectors, especially services. This sparked an outcry among investors that the doors were closing to foreign investment and some threatened to pull out their investments. Many investors complained pointedly that while Thailand was closing its doors, Vietnam had that same week joined the WTO and was opening wider to foreign investment. The implication was not subtle: investors were losing faith in Thailand and taking a fresh look at their neighbor, Vietnam.

¶3. Thai economic and business analysts have taken increasing note of Vietnam's reputation as a profitable destination for FDI and its growing prowess in export markets, and have expressed concern that Thailand will soon be surpassed economically by their dynamic neighbor. Vietnam's accession to the WTO, successful hosting of last year's APEC meetings, and continued strong economic growth have raised its global image and sparked substantial investor interest. Meanwhile, Thai business hit a rough patch in 2006 with political instability, a military coup, a rapidly strengthening currency that is hurting exports, and overall uneven economic management from the newly installed government.

¶4. Analysts fear that Thailand's traditional exports will face cut-throat competition from Vietnam's ever strengthening export sector, and that foreign investors will see the rapid growth, lower wages, and stable economy in Vietnam as a superior location for their investments. In a speech to a meeting of public and private sector leaders earlier last summer, former Deputy Prime Minister Somkid warned that unless Thailand boosted its competitiveness, Vietnam would overtake Thailand economically within five years. Kasikorn Research Center, a leading Thai economic analysis firm, predicted that Vietnam's exports would overtake Thailand's by 2020, and noted that foreign direct investment figures in Vietnam were already rapidly approaching those in Thailand.

Cooperation, not competition on trade

¶5. Vietnam and Thailand compete head to head on exports of rice, rubber, seafood products and apparel, among other goods. Faced with the economic challenge, Thai economic officials have taken to describing Vietnam not as a competitor but as a partner, and are working with the Vietnamese to prevent unbridled competition that

would lower prices for Thai exporters. Thailand and Vietnam have agreed to revive a Joint Trade Commission, now to be known as the Thailand-Vietnam Enhanced Economic Relationship, to discuss trade issues.

¶6. The Commission is planning its first meeting in February in Hanoi to discuss cooperation in rice trade. Combined the two countries account for approximately half the global rice trade, with the Thais controlling significantly more market share, but Thai exporters have complained that Vietnamese competition has held down prices. Last November, Thai and Vietnamese officials signed a Memorandum of Understanding on exchanging information on rice and price levels to stabilize rice prices, though both parties remain somewhat wary of sharing too much information. Thailand also pledged to assist Vietnam to improve its logistics system and warehouses so Vietnamese exporters would not be forced to dump rice on the global market at cut-rate prices because of an inability to maintain large stocks.

¶7. Thailand's rubber industry is also encouraging Vietnam, the world's fourth largest rubber exporter, to join the International Tripartite Rubber Organization, an organization set up by leading exporters Thailand, Malaysia and Indonesia to control price and supply. According to the Thailand Rubber Research Institute, Vietnam has agreed in principle to join the organization.

Vietnam vs. Thailand: Foreign investors weigh the scales
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¶8. Thailand's recent announcement of potential changes to foreign ownership requirements that could force foreign investors to give up majority control of their investments have created great unease among foreign investors, and Thai analysts have warned that Vietnam is quickly appearing more attractive for foreign investment in

comparison.

¶9. In general, Vietnam's primary competitor for foreign investment appears to be China rather than Thailand. Fred Burke, a lawyer at Baker & McKenzie in Ho Chi Minh City that handles much foreign investment work, told of significant amounts of direct and indirect foreign investment entering Vietnam, but said that incoming investors consider Vietnam as an alternative or back up to investing in China. Many investors have hedged their investments with a "China plus one" strategy, placing some investment in an ASEAN country to guard against any uncertainty or instability in the China market. It is notable that for these investors, Vietnam is grabbing the attention while Thailand slips from view. A U.S. construction firm operating in SE Asia said their demand for new commercial construction in Vietnam was booming; Thailand remained flat.

¶10. For investors who have substantial investments in both Thailand and Vietnam, Thailand maintains competitive advantages of its own that should keep much of its existing investment from drifting away to Vietnam, though new investment may be a different story. Management at a number of Singapore- and Thailand-based foreign companies with operations in both Thailand and Vietnam told Econoff that although they were enthusiastic about the potential of the fast growing market in Vietnam and the substantial profits already flowing from their investments there, they were not unduly discouraged by the investment environment in Thailand and noted advantages and disadvantages in each country. Panasonic (Matsushita Electronics) announced recently that it planned to move ahead with a six billion baht (USD 167 million) investment over three years despite market uncertainties. Panasonic cited Thailand's sizable domestic market, infrastructure and new airport, but also mentioned Vietnam would be another attractive market for its investments.

¶11. Vietnam holds an obvious advantage in lower labor costs, but Thailand frequently has certain advantages in material costs. One major apparel and shoe manufacturer noted that labor costs made up only 10 percent of their total production cost, input materials made up 65 percent. Thailand's mature supply structure and superior infrastructure helped keep these costs low. The manufacturer said Thailand remained a production source for a number of niche products

where the Thais maintained a large material base for inputs and in areas where they had higher skills and productivity, but noted the company was directing the vast majority of their new growth to Vietnam. A major food processor pointed out differing costs for land, tariffs, licenses, and logistics, giving Thailand the edge for better infrastructure and ease of doing business. The firm has growing investments in both Vietnam and Thailand, but made individual investment decisions on a case-by-case basis and did not necessarily have a preference for either one.

¶12. A private equity investor told Econoff that Vietnam had more attractive investment opportunities than Thailand, partly because the lack of investment in previous decades in Vietnam provided a bounty of possibilities for major investment. However, he warned that Vietnam was "hit and miss", and was riskier for small- and medium-sized investments, particularly in areas where few foreign investors had ventured. He considered Thailand a substantially less sexy market but safer and more predictable, with greater ease of doing business, less hassle from the government, and a better support structure of service providers such as accountants, bankers and lawyers.

If you can't beat 'em...

¶13. Not to be left behind, Thai firms have joined the gold rush, taking up 11th place on the list of Vietnam's largest foreign investors with 132 investment projects valued at USD 1.5 billion. In November, the Thai Ex-Im Bank visited Vietnam to provide greater support to Thai business there. In January Thailand's Board of Investment is planning a visit of Thai businessmen to seek out investment opportunities, focusing on tourism services, auto parts manufacturing and agro-industry processing. The potential competition for investment seems not to have struck BOI as serious; BOI has produced a slick CD on investing in Vietnam for Thai investors, but had no ready plan on how to prevent investment in Thailand from slipping to Vietnam.

¶14. Thailand maintains a healthy trade surplus with Vietnam, exporting approximately USD 3 billion to Vietnam through November this year, and importing USD 900 million over the same time period. Overall bilateral trade has more than doubled over the past three years, though Vietnam trade still accounts for only 1.5 percent of Thailand's total trade. More than half Vietnam's exports to Thailand consist of crude oil, computer parts and electrical machinery. Thailand ships back refined fuels and production inputs such as iron and steel, polymers, cement, and chemical and plastic products. Tourism has shot up as well, with the number of Thai visitors to Vietnam increasing by over 45 percent in 2006.

¶15. Comment: Thailand's dread surrounding the prospect of being "overtaken" by Vietnam is probably mostly psychological, Thailand

has more to gain from trade and investment with a prosperous neighbor than it would likely lose in exports and there are no clear signs yet that investment is slipping away from Thailand despite the concerns Thais recently expressed over the "loss" of a major Intel greenfield plant to Vietnam last year. Nevertheless, the sheer prospect is a much needed motivating factor for Thailand's government and business sectors to gear up for stronger competition. End Comment.
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